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IN THE

Supreme Court of the United States

October Term, 1947

No. 791

LILY HO QUON and ALBERT T. QUON,

Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE NINTH CIRCUIT.

Brief of Petitioners in Reply to Respondent's Brief in Opposition

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Brief of Petitioners in Reply to Respondent's Brief in Opposition.

1. Respondent's "Statement" Inaccurately Reflects the Tax Court's Findings of Fact Here.

A. The bona fides of the partnership here is an important factor in petitioners' case. Nowhere in its findings of fact—at not a single point—did the Tax Court utter any suggestion that the partnership was not bona fide. Yet, in several sentences otherwise drawn verbatim from those findings respondent has inserted his own qualifying adjective in reference to the partnership. Thus, on page 6 of his brief, 3rd line from the bottom, he has inserted the word "purported"; on page 7, line 10, the word

"alleged"; on page 8, 9th line from the bottom, the word "so-called"; and on page 9, line 16, again the word "so-called."

That the opinion of the Tax Court in this respect involves wholly a conclusion of law, and an erroneous conclusion of law, is shown in petitioners' brief in support of their petition, pages 17-22.

B. Another important factor in petitioners' case is that the income involved here is not attributable to petitioners, and is attributable to the limited partners because of their ownership of capital shares. Affecting that issue are these words of respondent, on page 8, line 6:

> "After his [taxpayer's] return from a business trip to China in August, 1940. . . ."

The Tax Court's findings of fact show, however, that taxpayer's trip lasted from April to August and that during that period "an employee named Fung was in *control* of the business and *operated* it." [R. 36—italics supplied.] This fact is important. The Tax Court in its opinion stated that the business was "operated" and "controlled" by the taxpayer prior to the formation of the partnership [R. 38]; also that for all practical purposes the business continued to be "operated" and "controlled" after the conversion to the partnership form in the same manner as before [R. 38-39]. The conclusion must be that the Tax Court was using the terms "operated" and "controlled" in a very general sense. It made no attempt to convey the impression, let alone to find directly, that the

business was dependent upon the taxpayer, nor that, as respondent charges in his argument (p. 14), any part of the income actually involved here was attributable to the "services, control and management" of the taxpayer. The Tax Court could only have meant that the taxpayer was in general charge of the business. So was the taxpayer in the *Feldman* case, cited by petitioners in their brief in support of the petition (p. 23). Here, moreover, the taxpayer was paid for his services, and nowhere did the Tax Court find, nor does respondent charge, that the compensation was inadequate.

2. Respondent's "Argument" Fails to Meet the Real Issues Involved Here.

A. Respondent in his argument (p. 13), states that "it is clear from the Tax Court's opinion [R. 38-40] that it was unable to find that a bona fide partnership had been created for federal income tax purposes." In attempting to distinguish the *Feldman* case, however, respondent (p. 14) pointed out that the trial court there had found as a fact that "a bona fide partnership had been created . . .", not that "a bona fide partnership had been created for federal income tax purposes. . . ." The resulting distinction is defective on its face. It begs the question of law as to the meaning of bona fides *for federal income tax purposes.*

In the *Feldman* case the trial court had found that the gifts were "bona fide, valid and irrevocable", that the donors ceased to be "the beneficial owners of the trust

property or the recipients of the income therefrom", and that none of the income or corpus of the trust was used for their "personal benefit or economic gain." On the basis of those findings, the Circuit Court of Appeals for the Fifth Circuit held that the partnership income allocated to the trust was not taxable to the donors. The Court there treated bona fides as a separate factor, as simply bona fides, and on the basis of all of these factors combined, reached its conclusion. All of these factors are as fully present in the case here as they were in the *Feldman* case. As petitioners pointed out, moreover, in their brief in support of the petition (p. 23), the case here contains several additional elements which make the petitioners' case even stronger. There is a clear conflict between the decision of the court below in this case and the decision of the court in the *Feldman* case.

B. Respondent in his argument (p. 12) also misstates the opinion of this Court in the *Tower* case. This Court did not say there that "unless the donee or assignee 'invests capital originating with her or substantially contributes to the control and management of the business, or otherwise performs vital additional services, or does all of these things', the Tax Court is justified in concluding that the donee or assignee is not a real partner for tax purposes." This Court only said that the Tax Court could "properly take these circumstances into consideration" in determining whether the partnership is real within the meaning of the federal revenue laws.

Here, of course, the limited partners rendered no services. That is just what limited partners as such are not supposed to do. As to contribution of capital, the shares which the limited partners owned were absolutely theirs; for as pointed out in petitioners' brief in support of the petition (pp. 15-16), any limited partner could terminate the partnership and withdraw his capital share. Respondent states in his argument, however (p. 14), that the capital "emanated" from the taxpayer or the marital community. In that he is attempting to engraft upon the federal income tax a wholly new theory—one that has no basis in principle and finds no support anywhere in the entire history of the federal income tax.

Conclusion.

Petitioners submit again that the decision below is erroneous, that it is in conflict with other decisions, both of this Court and other Circuit Courts of Appeals, and that the petition for a writ of certiorari should be granted.

Respectfully submitted,

GEORGE T. ALTMAN,

Attorney for Petitioners.

June 10, 1948.